No. 20,930

United States Court of Appeals

For the Ninth Circuit

San Francisco Mining Exchange,
Petitioner,

vs.

Securities and Exchange Commission,
Respondent.

On Petition to Review, Modify and Set Aside, and to Stay, an Order of the Securities and Exchange Commission

OPENING BRIEF FOR PETITIONER

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JURISDICTION

This case is before the Court on petition of the San Francisco Mining Exchange (herein sometimes called the "Petitioner") to review, modify and set aside, and to stay, an order of the Securities and Exchange Commission (herein called the "Commission"). The Commission's decision and order are reported as Securities and Exchange Act Release No. 7870.

This Court has jurisdiction under the Securities Exchange Act of 1934 as amended, 48 Stat. 881, 15 U.S.C. 78a., *et seq.* (herein called the "Act"), since petitioner was aggrieved by an order of the Commission (Securities and Exchange Act Release No. 7870), and has its prin-

cipal place of business in the United States Court of Appeals' Ninth Circuit.

STATEMENT OF THE CASE

I. THE FANTASTIC PRELUDE TO THE FILING OF FORMAL CHARGES AGAINST THE MINING EXCHANGE.

A. The Commission Staff Attempted to Importune the Members of the Mining Exchange Into a Voluntary Surrender of Its Registration.

Action preliminary to the administrative proceeding was initiated on July 11, 1962 when Arthur E. Pennekamp, the Regional Administrator of the Securities and Exchange Commission, came to the headquarters of the San Francisco Mining Exchange, conferred with the members of the Mining Exchange, and delivered to its Board of Governors a photostatic copy of a letter dated June 28, 1962 that he had received from the Director of the Commission's Division of Trading and Exchanges (one Philip A. Loomis, Jr.) (Tr., pp. 1496-1499).

At the July 11, 1962 conference, when Mr. Pennekamp delivered the copy of Loomis' letter to the Mining Exchange's Board of Governors, he also showed them a copy of a report prepared by the staff of the Commission entitled "Report on the San Francisco Mining Exchange—June, 1962—Non-Public—For Staff Use Only."

Within a few days—after clearing it with Washington—he delivered a copy of this Report to the members of the Mining Exchange for their study (Tr., pp. 1499-1502).

Because of the significance of Loomis' letter we set it forth in full at this first opportunity:

"*Airmail* June 28, 1962

Arthur E. Pennekamp, Esq.
Regional Administrator
Securities and Exchange Commission
821 Market Street
San Francisco 3, California

Re: San Francisco Mining Exchange

Dear Art:

The *Commission* has authorized us to proceed in the matter of the San Francisco Mining Exchange in accordance with our original plans. I understand also that you have received copies of the report on the Exchange as *revised in accordance with the Commission's directions.*

I suggest, therefore, that you arrange an appointment with the Board of Governors of the Exchange and then advise them, in effect, that the staff of the Commission has made a study of the San Francisco Mining Exchange as a result of which we have reached a firm conclusion that the registration of the San Francisco Mining Exchange as a national securities exchange, must be terminated. The staff recommendations have been *considered by the Commission.*

The normal consequence of this conclusion would be the initiation of a proceeding under Section 19(a)(1) of the Securities Exchange Act to withdraw the registration of the Exchange, and we are prepared to commence such a proceeding promptly. We feel, however, that the Exchange may wish to terminate its registration voluntarily in order to avoid the expense and embarrassment of public hearings.

If the Exchange wishes to take that course, it may submit withdrawal of its registration by July 15, and *the Commission* will order such withdrawal effective at an appropriate time.

The Exchange may also be advised that *the Commission does not plan* to make the report on the San Francisco Mining Exchange public at this time, but that copies are available for inspection by the Exchange. *The Commission does not wish,* however, to give copies of the report to the Exchange, since it might thereby lose control of the decision as to when and how this material might be made public.

If the Exchange withdraws its registration, it may give such reasons therefor as it sees fit, provided that they are not misleading. It should be understood, however, that while *the Commission does not plan* to make the report public at this time, the Commission may subsequently determine that it would be appropriate to do so, and the Exchange should not assume that *the Commission will not hereafter make the report,* and the reasons for the withdrawal of the Exchange's registration, public, in response to Congressional inquiry, or otherwise.

You may furnish a copy of this letter to the Exchange if you think that desirable.

If you have any questions about it, please let me know immediately when you have communicated this matter to the Exchange and when you receive any reaction from it.

Sincerely yours,
sgd Philip A. Loomis, Jr.,
Director''

Mr. Pennekamp insisted that during the July 11th conference at the Mining Exchange he urged the mem-

bers of the Exchange to obtain legal counsel to assist them in their consideration of the ultimatum presented in Loomis' letter (Tr., pp. 1497, 1550-1551). He knew that they did not have legal counsel (Tr., p. 1550). As a matter of fact, one of the eventual charges filed against the Mining Exchange was that:

> "The Exchange has retained no legal counsel for about 30 years and has not had adequate legal advice during this entire period." (Order for Public Proceedings, Par. II, E(4), page 11.)

3. Legal Counsel for the Mining Exchange Is Engaged—He Seeks a Conference With the Commission Staff Concerning Rehabilitation.

Legal counsel for the Mining Exchange first appeared on the scene on July 16, 1963, when its present counsel transmitted identical wires to both Loomis and the secretary of the Securities and Exchange Commission, one Orval A. Du Bois. Since this first statement of a legal position in behalf of the Mining Exchange sets forth clearly the attitude of legal counsel for the Mining Exchange, we quote the exact wire in full (Tr. pp. 2054-2056, Resp. Exh. 9):

> "Re: SAN FRANCISCO MINING EXCHANGE. SINCE MONDAY, JULY 16TH, I HAVE BEEN RETAINED AS LEGAL COUNSEL FOR THE EXCHANGE. HAD NO PRIOR KNOWLEDGE OF OR CONNECTION WITH ITS ACTIVITIES OR THOSE OF ANY SINGLE MEMBER. MET WITH A GROUP OF ITS MEMBERS YESTERDAY AND REVIEWED YOUR STAFF REPORT OF JUNE 12TH AND PHILIP LOOMIS' LETTER OF JUNE 28TH. CONFERRED THIS AFTERNOON WITH REGIONAL ADMINISTRATOR ARTHUR PENNEKAMP AND HIS STAFF. WAS ADVISED OF YOUR CONTEMPLATED WIRE ADVANCING FROM JULY 27TH TO 19TH THE DEADLINE FOR POSSIBLE VOLUNTARY WITHDRAWAL OF REGISTRATION.

MET LATER THIS AFTERNOON WITH GROUP OF MEMBERS AND AM AUTHORIZED TO ADVISE YOU AS FOLLOWS: (1)—IMPOSSIBLE FOR THEM TO REACH GROUP DECISION AS TO ADVISABILITY OF VOLUNTARY WITHDRAWAL BY THURSDAY DUE TO PRACTICAL CONSIDERATIONS. (2)—THEY ARE CALLING MEETING OF ALL MEMBERS FOR MONDAY, THE FIRST DAY WHEN ALL CAN BE PRESENT, TO REVIEW THE ENTIRE SITUATION IN OFFICIAL MEETING. PROBABLY WILL HAVE DEFINITE ANSWER BY LATE MONDAY OR TUESDAY. (3)—THEY ASSURE YOU THAT A DECISION TO SHUT DOWN EXCHANGE FOR WEEK'S VACATION WAS TAKEN WITHOUT LEGAL ADVICE BUT INTENDED AS COOPERATIVE ACT IN GOOD FAITH AND TO AVOID POSSIBLE CUSTOMERS' SUITS FOR FAILURE TO DISCLOSE DIFFICULTY WITH SEC. THEY ARE WILLING TO ACCEPT LEGAL ADVICE AS TO NECESSITY OF SUBMITTING TO COMMISSION SPECIFIC AND RIGID PLAN OF REHABILITATION, IF POSSIBLE TO BE PREPARED IN COOPERATION WITH COMMISSION STAFF. AM AUTHORIZED TO COME TO WASHINGTON FOR CONFERENCE WITH YOU OR STAFF MEMBERS IF IT WILL BE CONSTRUCTIVE. HAVE ADVISED EXCHANGE MEMBERS OF EXTREME GRAVITY OF SITUATION. AWAIT YOUR RESPONSE EITHER DIRECTLY OR THROUGH REGIONAL ADMINISTRATOR'S OFFICE."

C. The Commission Staff Refused to Discuss Rehabilitation.

Neither Loomis, the Director of the prosecuting Division of Trading and Exchanges, nor Du Bois, the Commission's secretary, acknowledged or answered the wire from the Exchange Counsel, but Loomis' Associate Director, one Irving M. Pollack sent a teletype message to Regional Administrator Pennekemp on July 18th. This message read as follows (Tr., p. 2057, Resp. Exh. 9A):

> "We have telegram from Gardiner Johnson, counsel for San Francisco Mining Exchange, stating it is impossible for Exchange members present in San Francisco to reach decision by July 19th as to advisability of voluntary withdrawal; that earliest pos-

sible date for meeting of all members is July 23rd, and they will have definite answer not later than July 24th; that closing of Exchange this week was intended to avoid possible civil suit for failure to disclose difficulty with SEC; and that *they want to submit specific plan of rehabilitation if possible* Stop We understand active members now running Exchange are available at this time Stop We shall withhold our recommendation to commission only if they assure us they are recommending to membership meeting on July 23 that registration be withdrawn and that Exchange does not intend to reopen Stop *Rehabilitation impossible.* Signed Irving M. Pollack, Associate Director, Division of Trading and Exchanges."

In spite of Associate Director Pollack's flat rejection of the suggestion of a proposed plan of rehabilitation of Mining Exchange procedures (his express words were: "REHABILITATION IMPOSSIBLE"), the members of the Exchange, under the guidance of their legal counsel (who had first been engaged only a week previously), proceeded to hold the promised meeting on Monday, July 23rd.

The members first voted against the suggestion that they voluntarily withdraw the registration of the Mining Exchange as a national securities exchange. Then, they proceeded to prepare and adopt a "plan of proposed operation of the Exchange which will relieve it from past criticism by the staff of the Commission."

On July 25th counsel for the Mining Exchange forwarded to Du Bois (the SEC secretary) a letter reporting in detail upon this meeting. A copy of the letter

went to Regional Administrator Pennekamp (Tr., pp. 2069-2083, Resp. Exh. 10). This was the letter of July 25th:

"In re: San Francisco Mining Exchange.

Dear Mr. Du Bois:

As you have probably been advised, on Monday, July 23rd, the members of the San Francisco Mining Exchange met to consider the suggestion that they agree to withdraw voluntarily the registration of the Exchange, as a national securities exchange.

After considerable discussion, the members present voted to declare themselves as opposed to the voluntary withdrawal of the registration and in favor of continuing operations as a national securities exchange.

Subsequently, the members of the Exchange adopted a formal resolution declaring themselves in favor of prompt preparation and submission to the Securities and Exchange Commission and its staff of a plan of proposed operation of the Exchange which will relieve it from past criticism by the Commission's staff, and conform to the suggestions heretofore made by the staff of the Commission.

This is to inform you that yesterday the first conference was held for the purpose of discussing and formulating such a plan of approved operation of the Exchange. A number of topics of suggested reform were discussed and specific proposals for improving operations were generally agreed upon. A second meeting is to be held later this week or early next week. It is anticipated that the plan will be completely formulated by the end of next week and the intention is to send it on to your office and to the

regional administrator's office for consideration, in the hope that discussion of the proposed plan might eventually eliminate much of the criticism heretofore leveled at the Exchange operations.

Among the topics discussed was a general review and modernization of the office administrative procedures of the Exchange. This topic will be discussed further at the next conference meeting. My purpose in sending this letter is to keep you and the regional administrator's office advised of these developments, so that you might be aware of the fact that the members of the Exchange are engaged in an effort in good faith to eliminate any of the past criticisms of their operations. Within the limited time available since I was retained, it has been my effort to try and aid very materially in bringing about such a program of a general revision of the form of the Exchange activities and operations.

We will keep you advised of developments in the immediate future.

Yours very truly,
Gardiner Johnson''

D. The Charges Are Filed in the Form of the ''Order for Public Proceedings.''

Secretary Du Bois answered under date of July 27, 1962 (Tr., pp. 2084-2087, Resp. Exh. 12) stating in part that:

''Prior to the receipt of your letter, the Commission issued an order for proceedings under Section 19(a) of the Securities and Exchange Act of 1934 to determine whether the registration of the Exchange should be withdrawn. A copy of this order is enclosed.

> "In view of the facts alleged by the Division of Trading and Exchanges, *it does not appear that any proposed plan of reorganization would obviate the necessity for going forward with these proceedings.*"

After the receipt of this letter from Du Bois, Regional Administrator Pennekamp advised the president of the Mining Exchange that further discussion of any program of rehabilitation was out of his hands (Tr., pp. 2091-2092).

The "Order for Public Proceedings" (which set forth the detailed charges against the Mining Exchange) was as reported in Du Bois' letter of July 27th, issued by him as Secretary of the Commission on July 26, 1962. They were promptly served by delivery of a copy to the president of the Mining Exchange.

Consistently since the first conference on July 11, 1962 the members of the Mining Exchange have refused to terminate voluntarily its registration as a national securities exchange.

II. COUNSEL FOR THE MINING EXCHANGE SOUGHT TO EXPLORE THE POSSIBILITY OF BIAS AND PREJUDICE BY INTERROGATING THE REGIONAL ADMINISTRATOR AND BY DEMANDING PERTINENT DOCUMENTS. FAILING TO OBTAIN ANSWERS OR DOCUMENTS HE REQUESTED SUBPOENAS DIRECTED TO THE MEMBERS OF THE COMMISSION.

A. Counsel for Petitioner Seeks to Question the Regional Administrator and States the Purpose of the Inquiry.

During cross-examination of Arthur Pennekamp, the SEC Regional Administrator, on February 5, 1963, he was asked by counsel for the Mining Exchange when he had

reported to Du Bois or Loomis concerning discussions with Archie Chevrier, a suspended member of the Mining Exchange. Immediately counsel for the Commission objected, claiming that:

> "This invades a province which under the recognizable standard is privileged. Conversations of that nature, internal conferences between staff members are privileged under the rule." (Tr., pp. 1535-1536).

The Hearing Examiner sustained the objection. The following colloquy then occurred:

> "Mr. Johnson: Mr. Hearing Officer, . . . may I state my purpose in pursuing this line of inquiry at this time?
>
> Hearing Examiner Ewell: Yes, sir.
>
> Mr. Johnson: Mr. Kennamer has objected previously, and I am aware, of course, that he intends to object to this question. I will state to the Hearing Officer that *among my purposes in pursuing this line of inquiry at this time generally is an effort to determine and demonstrate to the Hearing Officer whether or not this matter has been prejudged; whether or not the members of the Commission, members of the Securities and Exchange Commission of the United States*——
>
> Hearing Examiner Ewell: May I interrupt?
>
> Mr. Johnson: Yes.
>
> Hearing Examiner Ewell: *I don't think this is a proper line of discussion at this time,* until certain matters are clarified on the record, and in my own mind too. It doesn't seem to me that the objective that you mentioned is a proper one for presentation in this hearing.
>
> The Commission is not on trial here, and I don't think it appropriate for you to endeavor to make such

a demonstration; this is not a proper forum for it." (Tr., pp. 1536-1537).

There was further discussion of this problem of proof while Mr. Pennekamp was still under examination:

"Mr. Johnson: The point, Mr. Hearing Examiner, is this: I am pursuing this line of investigation with Mr. Pennekamp for the purpose of ascertaining by the questions that I have asked, and am about to ask, *whether or not this matter has in fact been prejudged by the Commission, by the consideration of evidence which is not part of the record, by consideration of matters which are actually extraneous to this hearing, and for the purpose of establishing by the competent testimony of those involved that the issue has previously been decided, and that we are in fact engaged in a pillow fight, an anticlimax, a consideration of facts which have in fact already been disposed of by the members of the Commission—*" (Tr., p. 1543, ll. 1-13).

and continuing:

"Mr. Kennamer: Now, Mr. Examiner, with respect to Mr. Johnson's contention that the proceedings regarding the San Francisco Mining Exchange have been, to use his term, I believe, 'prejudged,' I am not entirely certain whether he means prejudged by counsel for the Division, whether he means prejudged by the investigative staff, or whether he means prejudged by the Commission itself, or Mr. Examiner, by the Examiner who is presiding here.

These are loose and irresponsible accusations.

Hearing Examiner Ewell: In order not to broaden the thing unduly, Mr. Johnson, you may correct me if you think I am in error, but *the whole thrust of Mr. Johnson's remark, as I interpret it, is that the Com-*

mission itself has prejudged this case before the entry of the order, and did not refer to any particular division or office of the Commission.

Mr. Johnson: *That's correct.* May I say in support of your contention, *I used expressly 'the members of the Securities and Exchange Commission,'* and I did so deliberately. I certainly did not imply, and I trust it was not inferred that there was any accusation leveled at this hearing officer, and I am sure that the record would not support any such accusation. I was very careful in my statement to refer to the Commission.

Mr. Kennamer: May I finish my statement?

Mr. Johnson: All right.

Mr. Kennamer: With that interpretation, and with that narrowing of the charges that have been made here, I can only suggest, Mr. Examiner, that *none other than a member of the Commission could testify as to whether he has prejudged this matter.* Certainly Mr. Pennekamp can't explore the mind of any member of the Commission.

Now, if counsel for the Exchange makes such a contention, *the only avenue that I can suggest that might be available adjudication of this problem is a collateral suit against the members of the Commission.*

Hearing Examiner Ewell: *You mean in the courts.*

Mr. Kennamer: *Yes, sir; in the courts.*

Hearing Examiner Ewell: Well, I was going——

Mr. Kennamer: I don't believe the Hearing Officer could possibly make such a determination. I am certain that Mr. Pennekamp does not know whether any member of the Commission has reached a prior determination as to the merits of this proceeding.

Hearing Examiner Ewell: Well, I would presume it might be evidence if some other indirect statement about a Commissioner could be reflected in other ways,

but *my problem is as to whether that area is in any degree a proper subject for investigation.*" (Tr., pp. 1545-7).

B. Counsel for Petitioner Indicated That He Would Be Compelled to Request Subpoenas If the Information and Documents Were Not Forthcoming.

As counsel for the Commisison persisted in objecting to questions addressed to Mr. Kennekamp relative to his communications with the Commission concerning various facets of the Mining Exchange investigation, these objections were sustained. Counsel for the Mining Exchange then indicated that, failing to obtain the facts from Regional Administrator Pennekamp, he would probably have to request subpoenas for the members of the Commission. This was that discussion:

"Hearing Examiner Ewell: Well, no that wasn't quite what I had in mind. I said that after the testimony is all in on both sides, I wanted to know if you had any motions that you intended to make which would require a good deal of argument possibly, and study, before they could be disposed of.

Mr. Johnson: Let me clear up one point. Occasionally, Mr. Kennamer is helpful and surprisingly, I think on this occasion, he has raised a point that probably I should have cleared up in answer to your question. *This will depend to a considerable extent upon the nature of Mr. Pennekamp's testimony and the manner in which it is concluded, but there is a very serious possibility unless he changes or there is some change in his position it will be my intention to request subpoenas for members of the Exchange Commission. However, that is a matter I am going to have to appraise, as I go along.*

Mr. Kennamer: Well, I am glad that I have been helpful in this context, and I assume that counsel for the Exchange is now saying that he may or may not ask the Hearing Officer to issue subpoenas directed to the individual members of the Security and Exchange Commission." (Tr., p. 2105, l. 17 to p. 2106, l. 11.)

Upon further inquiry being made along the same line by the Commission's counsel, the position of the Mining Exchange was repeated:

"Mr. Kennamer: No, sir, but does that exhaust the number of witnesses who are to be called in concluding the case for the Mining Exchange?

Mr. Johnson: With the one exception that I noted previously in which *I said I would have to make the determination during Mr. Pennekamp's examination. I think that will not take too long,* and we will let you know right away.

Mr. Kennamer: Well, now, Mr. Examiner in the event that Mr. Pennekamp's testimony is not to the satisfaction of counsel for the Mining Exchange, I ask him now to identify the additional witnesses whose testimony might be needed.

Mr. Johnson: *I think I did, the members of the Commission, and possibly Mr. Du Bois. That would be it.*

Mr. Kennamer: In other words, you are now saying, sir, that *you may or may not request the attendance of the five members of the Securities and Exchange Commission, and the secretary of the Commission?*

Mr. Johnson: *That is correct. That is what I said before.*" (Tr., p. 2159, l. 15 to p. 2160, l. 8).

C. Counsel for Petitioner Made a Formal Demand for the Production of the Documents—It Was Held That They Were Confidential.

Upon Mr. Pennekamp's return as a witness he was asked to produce the correspondence that counsel for the Mining Exchange considered to be pertinent to his inquiry concerning possible bias or prejudice on the part of one or more Commission members. This was the question propounded:

"By Mr. Johnson:

Q. Mr. Pennekamp, will you produce, please, any correspondence in your files, either letters emanating from you, or your staff members in this regional office, or letters addressed to the members of the Commission, or the Securities and Exchange Commission, Mr. Orval Du Bois, or Mr. Philip A. Loomis, Jr., director of the Division of Trading and Exchanges, or any other member of the staff of the Securities and Exchange Commission in Washington, or any letters addressed to you or to members of your staff by members of the Commission, or by Mr. Orval Du Bois, the secretary of the Commission, or Mr. Philip A. Loomis, Jr., or Mr. Irving M. Pollack, associate director of the Division of Trading and Exchanges, or by any other members of the Commission's staff in Washington addressed to your office, or to any member of your staff during the following period: From March 27, 1962 to June 12, 1962, with relation to any of the following subjects, and with your permission, Mr. Hearing Officer, I am going to state them all so as to avoid having to ask repetitious questions on the proof that I have already referred to:

Communications on the following subjects: The transmittal of the statements made by Archie H. Chevrier on March the 27th and April the 11th.

The transmission of correspondence concerning the initiation of a comprehensive report and conduct of a comprehensive report with respect to the San Francisco Mining Exchange, any correspondence indicating or referring to the people, the members of the staff who prepared that report.

Any correspondence transmitting or referring to the transmission of documentary evidence or statements which were used in the preparation of that report.

Any correspondence relative to action taken by the Commission directing or suggesting revisions of the original draft of the report and indicating the extent to which it was revised and the nature of those revisions.

The next subject: Any correspondence relative to the question of offers on the part of the San Francisco Mining Exchange, its members, officers, or their legal counsel, to submit a plan of revision of their procedures between July 16, 1962, and September 4th, 1962; generally, any correspondence between March 27th and July 26th, 1962, relative to the initiation and filing of charges or an order for proceedings against the San Francisco Mining Exchange.

I would ask the production of those records." (Tr., p. 2187, l. 4 to p. 2188, l. 21).

After extensive argument, this was the disposition of the question:

"Mr. Kennamer: *The Division will not submit those communications, Mr. Examiner,* and I move that his question be stricken.

Hearing Examiner Ewell: Well, I will deny the motion. *I have already ruled that they were confidential, so I don't see any further discussion needed now.*" (Tr., p. 2193, ll. 17-21).

Mr. Pennekamp's testimony thereupon ended with this exchange:

> "Mr. Johnson: I have nothing more of Mr. Pennekamp at this time.
>
> Mr. Kennamer: Mr. Examiner, *I would like to inquire whether, now that Mr. Pennekamp has completed his testimony, counsel for the Mining Exchange intends to subpoena the individual members of the Securities and Exchange Commission.*
>
> Mr. Johnson: *Yes, he does.*
>
> Mr. Kennamer: Well, when is that application to be made, if it is to be made, Mr. Examiner?
>
> Mr. Johnson: I think I will make that with your permission on Monday.
>
> Hearing Examiner Ewell: All right." (Tr., p. 2194, l. 23 to p. 2195, l. 9).

D. Counsel for Petitioner Presented Written Requests for a Subpoena Duces Tecum and Subpoenas Ad Testificandum and Explored the Possibility of Their Issuance With the Hearing Examiner.

As promised, on Monday, February 11, 1963, counsel for the Mining Exchange presented to Hearing Examiner Ewell two written applications for the issuance of subpoenas. They were in the following form:

> (1) Affidavit and Application for Issuance of Subpoena Duces Tecum. (This requested only the issuance of a Subpoena Duces Tecum to Orval L. Du Bois, Secretary of the Commission); and
>
> (2) Application for Issuance of Subpoena. (This requested the issuance of subpoenas ad testificandum directed to the five members of the Commission).

Upon the presentation of the written applications by counsel for the Mining Exchange the following colloquy took place:

"Mr. Kennamer: Mr. Examiner, before we recess I would like to point out that under no circumstances can filing of these applications be considered as timely or suitable in these circumstances." (Tr., p. 2287, ll. 17-19).

"Hearing Examiner Ewell: I have given some thought to the matter, and while I agree that timeliness is a matter to be considered, *I think, as every lawyer knows, the facets of a lawsuit change from hour to hour. I don't think there is any precise limitation upon the moment of time at which a subpoena or the desirability of certain testimony or evidence might be deemed essential in the opinion of the counsel for the protection of his client, whoever he may be.*

So far as the subpoena duces tecum is concerned the rules require a showing of general relevance, which, of course, raises an issue that would require some sort of disposition prior to the issuance of the subpoena.

So far as the issuance of the subpoena ad testificandum is concerned, there is no special requirement other than an application, as far as that goes. However, I have some ideas on the subject that I intend to submit to the parties in due course. I would not want to do it until I had at least read the application for the subpoena duces tecum." (Tr., p. 2288, l. 18 to p. 2289, l. 10).

The position of the Mining Exchange counsel as to the procedure he was following was explained at page 2294, line 8 to page 2295, line 25, as follows:

"Mr. Johnson: *Subsection 1, it seems to me, does not require a written application.*

Hearing Examiner Ewell: *That is correct.*

Mr. Johnson: However, I put it in writing also because I was getting out the other one.

The wording of the section is, beginning with Section 1, 'Any member of the Commission, the Hearing Officer or any other officer designated by the Commission for the purpose, in connection with any hearing ordered by the Commission, Paragraph (i) shall issue subpoenas requiring the attendance and testimony of witnesses at any designated place of hearing, upon application therefor by any party.'

"Now, *in addition to the fact that a written application is not required, that subsection seems to say that upon an application being filed, a subpoena shall be issued; mandatory.* There is no requirement in that section or any statement or amplification in any sense.

Hearing Examiner Ewell: *Well, I think that is correct.*"

The Hearing Examiner stated clearly his understanding of the proper interpretation of the then controlling rule for the issuance of subpoenas ad testificandum:

"Mr. Kennamer: What has not been answered, Mr. Examiner, is the basis and fundamental inquiry, just what, if anything, does counsel for the Mining Exchange expect to prove from the testimony from all or any one of the five members of the Securities and Exchange Commission?

Hearing Examiner Ewell: *I don't think under the rules he is required—*

Mr. Johnson: That is my viewpoint.

Hearing Examiner Ewell: *It is mandatory without any qualification.*" (Tr., p. 2296, l. 25 to p. 2297, l. 9).

The legal situation as to the right of the Mining Exchange to obtain and present evidence of bias and prejudice on the part of members of the Commission was explored in the following discussion between Hearing Examiner Ewell and counsel for the Mining Exchange:

"Hearing Examiner Ewell: Do you have any reply to that, Mr. Johnson? I would like to have your expression of your position as to my suggested disposition.

Mr. Johnson: May I explore it with you a little bit?

Hearing Examiner Ewell: Yes, sir.

Mr. Johnson: I want to make sure that I understand it. If I understood your reading of the pertinent portions of the Federal Home Loan Bank case, the court in that matter, in effect, held two things: No. 1, they held that official responsibility or duty can't be shrugged off or divested by reason of the fact that even though they might be proved to be biased—in other words, it is incapable—the incumbent holders of memberships on Boards collectively are unable to divest themselves of the duty to proceed with a hearing——

Hearing Examiner Ewell: Yes, sir; apparently it says that the charges of bias and prejudice must give way to the necessity of permitting the same to perform its duty.

Mr. Johnson: In other words, for practical purposes, public business can't be held up. Even though you prove that all the members of a public board are biased and prejudiced, they must go ahead and conduct the hearing.

While that decision held that public business must proceed, it also held, and actually quite independently, that bias and prejudice and evidence of it is relevant

and that the Commission itself might consider whether or not one or more members of its body are biased and prejudiced.

Hearing Examiner Ewell: *I took that to mean that you could have introduced evidence in your case in chief, if you had it, that such a situation existed.*

Mr. Johnson: Well, that would permit us, *that would certainly give us a right to apply for subpoenas to prove that. We have applied for subpoenas.* I am not talking about for the moment about our subpoenas duces tecum. I am talking merely about the general one. We have applied for subpoenas, so even if we concede what Mr. Kennamer has been saying, namely that the only purpose is to explore into the question of bias and prejudice, then under that case we are entitled to the subpoena.

"Hearing Examiner Ewell: *Yes, I think you might have a prima facie right to it.*" (Tr., p. 2303, l. 1 to p. 2304, l. 15).

Ultimately the procedure for deciding the issue in a deliberative manner was agreed upon in this way:

"Mr. Johnson: On that point, Mr. Hearing Officer, I am gong to accede to your suggestion because in this matter, which I consider to be important, I am not going to put my client, or myself, in a position of trying to force a ruling in five or ten minutes on important issues such as this, and I think in fairness to you and everybody involved, you are entitled to time to research and think it over and come to whatever conclusion you will. Whatever you decide, we will comply with.

Hearing Examiner Ewell: So then *you would have no objection to my deferring the issuance of the subpoena or making disposition of this question until after I return to Washington?*

Mr. Johnson: *I certainly would not.*

Mr. Kennamer: And I assume, Mr. Examiner, there would be no objection to either the Mining Exchange or the Division addressing briefs to the Hearing Officer on the question as to whether the subpoena should be issued under the circumstances.

I might suggest that the Hearing Officer set a date within which such briefs might be received.

Hearing Examiner Ewell: That would seem to be appropriate, yes, sir.

How about ten days?

Mr. Kennamer: That's agreeable with the Division.

Mr. Johnson: That's all right with me, Mr. Hearing Officer. *I can tell you my brief will be the rule and the case you read from."* (Tr. p. 2310, l. 3 to p. 2311, l. 5).

III. THE HEARING OFFICER DENIED THE APPLICATION FOR A SUBPOENA DUCES TECUM, BUT GRANTED THE APPLICATION FOR SUBPOENAS DIRECTED TO THE MEMBERS OF THE COMMISSION! THE COMMISSION REVERSED THE ORDER DIRECTING THE ISSUANCE OF SUBPOENAS TO ITS OWN MEMBERS.

A. The Application for a Subpoena Duces Tecum Directed to the Secretary Was Denied.

On March 15, 1963 the Hearing Examiner issued a lengthy "Memorandum and Order on Application for Issuance of Subpoenas" in which:

1. "It is Ordered that the application for issuance of a subpoena *duces tecum* directed to Orval L. Du Bois, Secretary of the Commission, for production of the material set forth therein be, and the same hereby is, DENIED." and

2. "Deferment of a ruling on the application for issuance of the subpoena *ad testificandum* until after the within ruling on the subpoena *duces tecum* had become final upon review would not be prejudicial to the parties."

The Mining Exchange excepted to the first ruling and applied for its certification to the Commission. On April 2, 1963 the Hearing Examiner certified the exceptions for review. On July 31, 1963 the Commission issued its "Memorandum Opinion and Order" which concluded with this direction:

"Accordingly, It is Ordered that the ruling of the hearing examiner refusing to issue a subpoena *duces tecum* requested by the Exchange in this proceeding be, and it hereby is, affirmed."

A rehearing was requested, but it was denied on September 9, 1963.

B. The Application for Subpoenas Ad Testificandum Directed to the Members of the Commission Is Granted.

On September 10, 1963 Hearing Examiner James G. Ewell issued his "Ruling and Order On Application for Certain Subpoenas Ad Testificandum." The effective part of the order was the direction that the application:

"is hereby *GRANTED.*"

The Hearing Examiner, having considered thoroughly the positions stated by the parties, came to this conclusion:

"Now, therefore, upon consideration of the foregoing, the briefs heretofore submitted and the principles set forth in the memorandum and order of the undersigned dated March 15, 1963, aforesaid, indi-

cating that, under the provisions of Rule 14(b)(1)(i) of the Commission's Rules of Practice, *issuance of subpoenas ad testificandum under application of any party is mandatory, the pending application for issuance of subpoenas directed to each member of the Commission and to its Secretary to appear and testify in this proceeding at the instance of counsel for the respondent, is hereby GRANTED; said subpoenas to be made returnable at such time and place as may hereafter be agreed upon by the parties, and*

It is so ORDERED.''

The result was that the petitioner herein, the Mining Exchange, was then entitled to subpoenas directing the five members of the Commission to appear and be examined. Hearing Examiner Ewell's letter of transmittal stated that he had left open for further discussion the time and place for the resumption of the taking of testimony.

C. The Commission Reversed the Order for the Issuance of Subpoenas Directed to Its Own Members.

As might have been expected, the Division of Trading and Exchanges was not satisfied with the Hearing Examiner's order. The Division took exception to the ruling and order on September 13th, and requested that the question be certified to the Commission for review. The Hearing Examiner certified the question on September 25th.

More than five months later, on February 26, 1964, the Commission finally issued its ''Memorandum Opinion and Order'' stating:

> ''It is Ordered that the ruling of the hearing examiner granting the request of the Exchange for issuance of subpoenas ad testificandum be *reversed,* and that *such subpoenas not be issued.''*

IV. REASONABLE GROUNDS EXISTED FOR INQUIRING INTO THE POSSIBLE BIAS OR PREJUDICE OF ONE OR MORE MEMBERS OF THE COMMISSION. APPLICABLE LEGAL AUTHORITIES HOLD THAT PETITIONER WAS ENTITLED TO THE ISSUANCE OF SUBPOENAS SO AS TO AFFORD IT AN EVIDENTIARY HEARING ON THE ISSUE OF BIAS AND PREJUDICE.

A. Several Grounds Existed That Supported the Belief That Some Members of the Commission Were Not Objective in Their Consideration of the Proceeding.

The administrative record developed a number of specific facts suggestive of the possibility that one or more of the Commission members had not maintained that objectivity that conforms to the traditional view of an impartial and disinterested tribunal.

In the first place, the Loomis letter of June 28, 1962 was replete with references to:

> "the *Commission* has authorized us to proceed;"
>
> "*revised in accordance with the Commission's directions;*"
>
> "*staff recommendations have been considered by the Commission . . . ;*"
>
> "*the Commission* will order such withdrawal;"
>
> "*the Commission* does not plan;"
>
> "*the Commission* does not wish;"
>
> "*the Commission* does not plan to make the report public;"
>
> "*the Commission* will not hereafter make the report . . . public."

Secondly, more compelling, and cumulatively suggestive of a lack of objectivity and impartiality, was the generally known fact that two of the five members of the Commis-

sion had served for almost twenty years each in various capacities as members of the SEC staff. Their records of SEC staff services are recorded in the following biographies from "Who's Who in America" (Vol. 34, 1966-67):

Cohen, Manuel Frederick: govt. ofcl.; b. Bklyn., Oct. 9, 1912; s. Edward and Lena (Katzmar); C.; B.S. in Social Sci., Bklyn. Coll. 1933; LL.B. cum laude St. Lawrence U., 1936; m. Pauline Grossman, Apr. 20, 1940; children—Susan D., Jonathan W. Research asso. 20th Century Fund, 1933-34; admitted to N.Y. bar, 1937; pvt. practice, N.Y.C. 1937-42; *with SEC, 1942—, chief counsel div. corp. finance, 1952-59, adviser to comm., 1959-60, dir. div. corp. finance, 1960-61, commissioner, 1961—, chairman and secretary, since 1964*——. Lecturer in law George Washington U. Law School, 1958——; mem. council Adminstrv. Conf. U.S., 1961——. Recipient Rockefeller Pub. Service award, 1956, Nat. Civil Service League Career Service award, 1961. Mem. Am. Fed. bar assns., Am. Soc. Internat. Law, Author articles profl. Jours Home: 6403 Marjory Lane, Bethesda 14, Md. Office: Securities and Exchange Comm. 425 2d St. N.W., Washington 25.

Woodside, Byron Darlington: govt. ofcl.; b. Oxford, Pa., Aug. 28, 1908; s. Crosby J. and Bertha Taylor (Frame) W.; B.S.; U. Pa., 1929; A.M., George Washington U., 1933, grad. study, 1937-42; LL.B., Temple U., 1946; m. Georgette Frances Ingram, Jan. 30, 1932; children—Byron C., Billie (Mrs. John C. Patterson), Georgette Merilyn, Admitted to D.C. bar, 1950; *asst. dir. div. corp. finance SEC, 1940-48, 49-50, asso. dir., 1952, dir. div. corp. finance, 1952-60, mem. SEC, 1960——;* dir. bus. expansion office NSRB, 1950-51; dir. div. def. expansion, Office Resources Expansion,

DPA, 1951. Mem. deconcentration review bd. G.H.Q., SCAP. U.S. Army, Tokyo, Japan, 1948-49. Mem. Phi Delta Phi. Home: Haymarket, Va. Office: 425 2d St. N.W., Washington 25.

Many of the facts referred to in the charges as constituting violations occurred during the years when Messrs. Cohen and Woodside were active members of the staff, and prior to their respective appointments to membership on the Commission.

B. Counsel for Petitioner Followed the Course of Attempting to Make Inquiry Before Filing Charges of Bias and Prejudice.

Knowing of these specific facts suggesting the possibility of non-objectivity on the part of one or more Commission members, and being aware that the disqualification of regulatory agency members has become increasingly frequent in the administrative process, counsel for the Mining Exchange was justified in taking steps to protect his client against a biased commission whose members, or some of them, had prejudged the issue, and who would consider the record with closed minds.*

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*See 25 *Fed. Bar Journal* 273, Paul Rand Dixon, chairman Federal Trade Commission: "Disqualification of Regulatory Agency Members: The New Challenge to the Administrative Process". Pertinent is this portion of the Introduction:

> "A major problem now seems to be developing, however, around that vital phrase 'informed by experience.' The question is being raised as to whether agency members can be so well 'informed by experience' that *their minds are already closed before particular cases reach them for adjudication—whether* they have, in short, 'decided in advance' the issues involved and are, therefore, 'disqualified' to hear and adjudicate those matters. In recent weeks the agencies and the courts have been presented with a rash of 'bias' cases."

Counsel followed the cautious, responsible course of making inquiry first, rather than hurling loose charges of bias and prejudice. He made clear the purpose of his inquiry upon cross-examination of Regional Administrator Pennekamp (Tr. pp. 1535-7) during the presentation of the Division's case (before the Mining Exchange had an opportunity to undertake its own affirmative presentation).

When objections to this line of inquiry were sustained, and Mr. Pennekamp was allowed to leave the witness stand without either producing the documents that were requested or answering the questions that were propounded, counsel for the Mining Exchange stated that, if the necessary evidence was not forthcoming from Mr. Pennekamp, he would probably request subpoenas for the members of the Commission and their Secretary (Du Bois). This statement was made at several points in the record (Tr., pp. 2105-6; pp. 2159-60).

As soon as Mr. Pennekamp's testimony was completed during the presentation on the part of the Mining Exchange, its counsel stated positively that he would present applications for subpoenas for members of the Commission at the next session. That was done.

As is clearly evident from a reading of the excerpts from the transcript that are pertinent to this issue, it was the theory of counsel for the Mining Exchange that the rules and the reported decisions pointed out that the approved course of action is to raise the question of bias and prejudice during the administrative hearing, make known the purpose of the inquiry, then request sub-

poenas if necessary, and request an evidentiary hearing upon the issue of bias and prejudice as part of the administrative process.

On the contrary, counsel for the Division adamantly maintained that:

> ". . . The only avenue that I can suggest that might be available adjudication of this problem is a collateral suit against the members of the commission in the courts." (Tr., p. 1546)

C. The Effect of the Commission's Order Reversing the Hearing Examiner's Direction That Subpoenas Ad Testificandum Be Issued Was to Deny Petitioner Due Process of Law.

The effect of the Commission's order reversing the Hearing Examiner's Ruling and Order *granting* the application for the issuance of subpoenas *ad testificandum* was to deprive the Mining Exchange of the requested evidentiary hearing on the issue of bias and prejudice on the part of one or more of the Commissioners.

The San Francisco Mining Exchange, petitioner herein, has consistently asserted that this ruling deprived it of a fair and full hearing and constituted a denial of due process of law.

D. The Commission's Own Footnote 19 to Its "Findings and Opinion" Is Clear Evidence of Its Apprehension That It Has Denied Petitioner Due Process of Law.

So strong is the record in support of petitioner's charge of a denial of due process of law that the Commission itself was unable to refrain from the expression of a note of apprehension in an entirely defensive, although indefensible, footnote to its "Findings and Opinion of the Commission" dated April 22, 1966. Having concluded

that it would withdraw the registration of the Mining Exchange, it wound up its Opinion with this sentence:

> "The withdrawal of its registration is, if anything, long overdue.[19]"

The Commission could not resist adding that footnote 19. It is a self-exculpatory, entire defensive restatement of its pretext for denying a full evidentiary hearing on the sensitive issue of the bias and prejudice of one or more of its own members. This is the full footnote 19:

> "The Exchange in its brief in support of the hearing examiner's recommended decision states that if his recommendation is not approved by us, its position is that *it has been denied a full and fair hearing because of our refusal to authorize the issuance of subpoenas directed to the members of this Commission and our Secretary* and for the production of non-public Commission files, all allegedly for the purpose of inquiring into whether this Commission was biased or had prejudged the issues against the Exchange. We have already considered and rejected these contentions of the Exchange on three prior occasions. Securities Exchange Act Release No. 7106 (July 31, 1963); Securities Exchange Act Release No. 7247 (February 26, 1964). We see no reason to change our conclusions in this respect and for all the reasons stated in our prior rulings we affirm them. Nothing has been presented to indicate that the Exchange has not had a fair hearing. In fact, as we previously noted (Securities Exchange Act Release No. 7106, p. 2) in view of the nature of these proceedings we authorized the Division to take the unusual step of furnishing the Exchange a copy of the Division's investigation report prior to the institution of these proceedings. Our decision herein

is based solely on the facts in this record, many of which have been admitted by the Exchange and most of which are uncontroverted."

E. The Controlling Legal Authorities Support Petitioner's Contention That It Was Entitled to the Issuance of Subpoenas so as to Afford It an Evidentiary Hearing on the Issue of Bias and Prejudice.

The obvious apprehension and anxiety of the Commission as it is made apparent in footnote 19 to the "Findings and Opinion of the Commission" is easily understood when one turns to the reported decisions on the subject of the disqualification of regulatory agency members for bias and prejudice—especially decisions involving the present chairman of the Securities and Exchange Commission, Manuel F. Cohen, one of those whom counsel for the Mining Exchange sought to subpoena and question.

One of the early landmark decisions was rendered in the Third Circuit in 1941 in the case of *Berkshire Employees Association v. National Labor Relations Board,* 121 Fed. 2d 235, 238-9, in which Judge Goodrich wrote the opinion including this historic statement of the essential elements of fair play in the functioning of an administrative tribunal:

> ". . . If the administration of public affairs by administrative tribunals is to find its place within the present framework of our government it is essential that it proceed, on what may be termed its judicial side, without too violent a departure from what many generations of English speaking people have come to regard as essential to fair play. One of these essentials is the resolution of contested questions by

an impartial and disinterested tribunal. These adjectives are not absolute but relative as every thoughtful person knows. Decisions affecting human beings, made by human beings, necessarily are colored by the sum total of the thoughts and emotions of those responsible for the decision. The Judicial process, or any other human process, cannot operate in a vacuum. The most we can hope for is that persons charged with the responsibility for decisions affecting other people's lives and property will be as objective as humanly possible. Certain rules, of more or less definiteness, have been worked out through judicial decision by judges to regulate their own conduct.

* * *

"We conclude that in this case the facts, if proved, show a case which goes beyond the line of fair dealing with a particular litigant. If the circumstances alleged are proved Berkshire did not have a hearing before an impartial tribunal, but one in which one member of the body which made exceedingly important findings of fact had already thrown his weight on the other side. This is obviously not like a case where ill-advised extrajudicial statements have been made by a judge, or where a litigant seeks to subject an administrative body to interrogatories to discover the inner workings of the administrator's mind. It goes further and, in our judgment, it goes beyond that which is permissible from the standpoint of either litigants or public.

"The Board argues that at worst the evidence only shows that one member of the body making the adjudication was not in a position to judge impartially. We deem this answer insufficient. Litigants are entitled to an impartial tribunal whether it consists of one man or twenty and there is no way

> which we know of whereby the influence of one upon the others can be quantitatively measured."

That classic delineation of administrative objectivity has been repeated approvingly time and again, including a case involving both the Securities and Exchange Commission and the conduct of the present chairman and long-time staff member, Manuel F. Cohen (one of the members that petitioner in this proceeding sought to subpoena and examine).

In that case, *Amos Treat & Co. v. Securities and Exchange Commission* (1962) 306 Fed. 2d 260, 263, Justice Danaher of the District of Columbia Circuit wrote the opinion. As he pointed out, the appellant Treat had filed a motion that "an evidentiary hearing be held to determine whether any members of the Commission were disqualified with respect to past or future proceedings and the facts relating to the ex parte representations, so as to enable the Commission to then determine whether to grant a discontinuance."

The Commission denied the motion to adduce further evidence on the facts. In the *Treat* case, as in the instance of footnote 19 in this proceeding, the Commission's state of apprehension was evident, and:

> "Appended to the Commission's April 11, 1962 'minute' order was a written statement prepared by Commissioner Cohen outlining his recollection and conclusions with respect to the various proceedings which had been conducted while he was the director of the Division of Corporation Finance and stating the extent to which he had participated in the actions taken by the Commission." (At p. 263)

The Court of Appeals for the District was unimpressed by Commissioner Cohen's ex parte effort at self-exculpation. In ruling it said:

"Appellants alleged that participation by Commissioner Cohen had rendered the proceedings void and so irrevocably tainted that any final determination which might flow from such proceedings will be invalid. It is our view that a substantial showing has been made.

Just exactly how the concept of 'due process' is to be applied will vary with the type of proceeding involved, as we are well aware.

'Its exact boundaries are undefinable, and its content varies according to specific factual contexts. Thus, when governmental agencies adjudicate or make binding determinations which directly affect the legal rights of individuals, it is imperative that those agencies use the procedures which have traditionally been associated with the judical process.'

"At the very least, quasi-judicial proceedings entail a fair trial. As the Supreme Court has said in other context:

'A fair trial in a fair tribunal is a basic requirement of due process. Fairness of course requires an absence of actual bias in the trial of cases. But our system of law has always endeavored to prevent even the probability of unfairness.

* * * * *

'It would be very strange if our system of law permitted a judge to act as a grand jury and then try the very persons accused as a result of his investigations. * * * Having been a part of that process a judge cannot be, in the very nature of things, wholly disinterested in the conviction or ac-

> quittal of those accused. * * * Fair trials are too important a part of our free society to let prosecuting judges be trial judges of the charges they prefer.' " (at p. 263)

The same general reasoning prevailed in the decision rendered by this Court in *Federal Home Loan Bank Board v. Long Beach Federal Savings & Loan Association* (1961) 295 F. 2d 403. This was the case studied by Hearing Examiner Ewell when petitioner presented its applications for subpoenas, and it was the subject of the exploratory colloquy between the Hearing Examiner and counsel for the Mining Exchange (Tr., pp. 2299-2304), during which counsel outlined his understanding of the approved procedure for obtaining an evidentiary hearing upon a prospective claim of bias and prejudice.

The following portions of the *Federal Home Loan Bank* case seem pertinent to this proceeding and actually are controlling on the issue here presented (at pp. 408-409):

> "In our opinion, however, a majority of the Board members were without power to disqualify themselves for bias or prejudice, although possibly an individual member comprising a minority of the Board could have done so. The charge of bias and prejudice directed against the majority of the members of a government agency must give way to the necessity of permitting the agency to perform the function which it alone is empowered to perform.
>
> It follows that no action the Board could have taken on the Association's challenge as to the qualifications of its members could have resulted in the invalidation of previous Board orders and thus undermined the legality of the subpoenas. Nor could any

such action have disabled the Board, or a majority thereof, from performing its statutory duties at all future stages of the proceeding. Hence the district court should not have directed the Board to act on the challenges nor should it have stayed action on the enforcement petition pending such a Board determination.

But while the charges of bias and prejudice on the part of the Board and its members could not operate to undermine the authority under which the Board issued the subpoenas, evidence of bias and prejudice the Association thereby sought to produce was not irrelevant. In connection with the presentation of the Association's case-in-chief, as the examiner properly ruled, the Board should receive evidence of bias and prejudice on the part of its members. Such evidence would be relevant because the Board could determine for itself whether if the facts are established, a minority member is disqualified from participation in the final decision. Berkshire Employees Ass'n of Berkshire Knitting Mills v. N.L.R.B. 3 Cir., 121 F. 2d 235, 239. *Evidence of bias or prejudice on the part of Board members would also be relevant for consideration by a court called upon to review a final Board order.* See Marquette Cement Mfg. Co. v. F.T.C., supra note 9, 147 F. 2d at page 594."

In that case, the appellant association, during the administrative hearing, had applied to the examiner for subpoenas addressed to the members of the Board and other persons. The Examine issued the subpoenas as requested. The members of the Board filed a motion to quash them, which was denied.

The reported decisions support the conclusion of Hearing Examiner Ewell that petitioner was entitled to an evidentiary hearing to explore the possibility of bias and prejudice on the part of one or more of the members of the Commission, and that subpoenas ad testificandum should have been issued.

The Commission's "Memorandum Opinion and Order" of February 26, 1964 reversing the Hearing Examiner and directing that "such subpoenas not be issued" was contrary to law, denied to petitioner a fair and full hearing, and was a denial of due process of law.

F. The Commission's Attempt to Wrap the Cloak of Confidentiality Around Documents Pertinent to a Litigated Controversy Is Contrary to the Prevailing Federal Rule.

Petitioner's "Affidavit and Application for Issuance of Subpoena Duces Tecum" directed to the secretary of the Commission (Du Bois) was denied by the Hearing Examiner in his "Memorandum and Order on Application for Issuance of Subpoenas" dated March 15, 1963 with the conclusion that:

> "* * * All of such material is deemed to come squarely within the meaning of the Commission's rule announcing *the confidentiality* of such material and prohibiting its disclosure without the Commission's approval--even by persons under subpoena. The applicable provision on this point is set forth in Rule 26(c) of the Commission's Rule of Practice." (at p. 12)

In support of its "Affidavit and Application for Subpoena Duces Tecum" petitioner filed with the Hearing Examiner a Brief citing two leading authorities from the

Federal Courts setting forth masterly statements of the modern rule frowning upon government efforts to set up, by rule or otherwise, the protective screen of "confidentiality" around pertinent documents, and thereby seek to suppress them.

We referred to the opinion by Justice Learned Hand in *U. S. v. Andolschek* (1944) 142 F. 2d 503, 506, where he said (in a criminal case):

> "While we must accept it as lawful for a department of the government to suppress documents, even when they will help determine controversies between third persons, we cannot agree that this should include their suppression in a criminal prosecution, founded upon those very dealings to which the documents relate, and whose criminality they will, or may, tend to exculpate. So far as they directly touch the criminal dealings, the prosecution necessarily ends any confidential character the documents may possess; it must be conducted in the open, and will lay bare their subject matter. The government must choose; either it must leave the transactions in the obscurity from which a trial will draw them, or it must expose them fully."

To the same effect was the opinion of Mr. Justice Brennan in the famous case of *Jencks v. United States* (1957) 353 U.S. 657:

> "We hold that the criminal action must be dismissed when the Government, on the ground of privilege, elects not to comply with an order to produce, for the accused's inspection and for admission in evidence, relevant statements or reports in its possession of government witnesses touching the subject matter of their testimony at the trial. Accord, Rori-

> aro v. United States, 353 U.S. 53, 60-61, 77 S.Ct. 623, 627-628, 1 L.Ed.2d 639. The burden is the Government's, not to be shifted to the trial judge, to decide whether the public prejudice of allowing the crime to go unpunished is greater than that attendant upon the possible disclosure of state secrets and other confidential information in the Government's possession."

While the *Jencks* case was criminal in nature, the *Jencks* doctrine has been recognized as applying to the administrative process. This was enunciated in *Great Lakes Airlines v. C.A.B.,* 291 F. 2d 354-362, as follows:

> "* * * The underlying principle of the Jencks case is generally applicable in administrative proceedings and has been judicially recognized."

Hearing Examiner Ewell conceded of the *Jencks* case, that:

> "It is clear, also, that the principle therein announced would tend to reach documents of virtually every kind, in the hands of government officials * * *."

He felt, though, that until the Commission had taken action and such action has been "made known the undersigned considers the Rule—(26c)—to be binding upon the Hearing Examiner at all times during the conduct of a proceeding in which he has been designated to function."

Certainly the United States Court of Appeals is under no such compulsion. It should recognize that the salutary rules of the *Jencks* case should apply to the Securities and Exchange Commission equally as to a criminal case.

V. THE CONCLUSION AND REMEDY RECOMMENDED BY THE HEARING EXAMINER ARE SUPPORTED BY THE RECORD OF THE PROCEEDINGS AND THE RECORD OF PERFORMANCE BY THE MINING EXCHANGE—THE ORDER OF THE COMMISSION SHOULD BE SET ASIDE.

A. The Hearing Examiner's Conclusion Was Based on a Careful Consideration of Uncontradicted Testimony.

Hearing Examiner James G. Ewell reviewed carefully the entire transcript of the proceedings and then set forth in his "Recommended Decision" a detailed series of Findings of Fact numbered from 1 to 118.

The Hearing Examiner took a severe attitude concerning the omissions, as well as both the misfeasance and malfeasance of the members of the Mining Exchange. He made findings in accordance with the stipulations, the exhibits and the oral testimony.

Having completed his findings, he then proceeded to weigh the evidence—all of it—in determining the appropriate remedy. Considering the entire record, which he had heard and read personally, he reached the conclusion set forth at page 106 of the "Recommended Decision", which was:

> "The undersigned therefore concludes, in exercise of what is believed to be due moderation, that the public interest (indeed, as here attempted to be expressed by responsible persons of high office and by recognized professional and civic bodies) might well be served if the present officials of the Mining Exchange were afforded a further but final opportunity under the guidance of their counsel, to reorganize the Mining Exchange in all of its functional aspects so as to present entirely new personnel in every department of management without exception."

In reaching his conclusion and determining upon the nature of the remedy, the Hearing Examiner was impelled to accept the uncontradicted and unchallenged testimony of independent, impartial witnesses produced by the Mining Exchange, whose only purpose and motive was a desire to serve the public welfare and to speak and act in the public interest.

He made this clear in the preliminary portions of his "Conclusions and Recommendations," when he said (at pp. 104-105):

> "In sum, the evidence on behalf of respondent in the form of opinions of public bodies and officials although, as already pointed out, susceptible of weakness inherent in all hearsay testimony, nevertheless is regarded by the Examiner as worthy of consideration—inasmuch as there is no evidence of demonstrable self-interest or any motive other than a desire, on the part of the givers of the testimony, to serve the public welfare.
>
> "* * * It would seem to follow that the opinions of the public bodies and officials placed upon the record here are entitled to be considered substantial evidence at least of the *reputation* of the Mining Exchange as having rendered valuable service to the Mining industry in the community in which it has operated for more than 100 years."

The evidence from public officials and public bodies referred to in the Hearing Examiner's "Conclusion and Recommendations" was summarized and accepted by him in his Findings 115-118 (pages 97-104 of the "Recommended Decision.")

This evidence presented by the Mining Exchange was not contradicted or challenged in any way by the prosecuting Division of Trading and Exchanges. Its counsel contented himself with scoffing at it as "totally lacking in evidentiary value." (Tr., pp. 2256, 2266)

B. Responsible Public Officials and Recognized Professional and Civic Bodies Urged That the Mining Exchange Be Allowed a further Opportunity to Reorganize.

One of the most impressive witnesses was Philip R. Bradley, a mining engineer, who had served for 19 years as Chairman of the State Mining Board. He presented and read into the record an official resolution adopted by the California State Mining Board on December 12, 1962. It read as follows:

> "*San Francisco Mining Exchange:* Discussed effects of closing the Exchange, as is being contemplated by the Securities and Exchange Commission. The Board authorized the following resolution: Resolved, that the State Mining Board recognizes the need and value of a Stock Exchange such as the San Francisco Mining Exchange, and is in sympathy with the furtherance of such an Exchange, provided that it operates within the regulations of the Security (sic) Exchange Commission, and that any irregularities within the Exchange be corrected."
>
> (See Finding 116, p. 99 of Recommended Decision for testimony of Philip R. Bradley, see Tr., pp. 1666-1677.)

Equally strong was a resolution read into the record by G. Louis Fox, Executive Vice President of the San Francisco Chamber of Commerce. This resolution had

been adopted by the Chamber's Board of Directors upon the recommendation of its Mining Committee. The resolution stated, in part:

> "On recommendation of the Mining Committee of the San Francisco Chamber of Commerce, the Chamber's Executive Committee strongly supports retention of the San Francisco Mining Exchange as an institution which has rendered, and should continue to provide, essential services in the development of the mineral resources of the State of California and the West by making possible the financing of small mining enterprises. . . .
>
> "The Mining Committee believes that the *San Francisco Mining Exchange has rendered and should continue to render essential services by making possible the financing of small mining enterprises whose stocks do not qualify for trading on the regular Stock Exchange.* It seems unnecessary to point out that virtually all the large producing mining enterprises of the nation have sprung from ventures that were initially very small.
>
> "In the event of the closing of the Mining Exchange it might be possible for small companies to market securities elsewhere, but it is suggested that in the marketing of the stocks through other channels protection of the investing public will be lessened, in contrast to the SEC's aim of increasing this protection. To count on the distribution of the stocks of member companies through other channels or through mining exchanges in cities distant from the headquarters of these firms would interfere, probably fatally, with the distribution of the securities of the small enterprises involved." (Tr., pp. 1539, 1560-61)

Strong statements were presented in the form of letters from George Christopher, then the Mayor of San Francisco (set out in full in Finding 117) and from the then Congressman Jack Shelley, now the Mayor of San Francisco (Finding 118).

The Governor of the State of Nevada, Honorable Grant Sawyer, submitted an unusually strong statement pointing out the unique contributions of the Mining Exchange to the mining industry of the entire West. In part, Governor Sawyer said this:

> "Because of the importance of this Exchange to the already depressed mining industry in Nevada and because of the reliance of many small mining enterprises in this state on the services of the Exchange, I am writing to request that further consideration be given before making your final decision.
>
> "The San Francisco Mining Exchange has been in operation for almost one hundred years, and in its history, has made a unique contribution to the development of the western mining industry.
>
> "The existence of an exchange close to Nevada which can provide marketing services is of great importance * * *. The San Francisco Mining Exchange, both because of its geographical location and its specialized services, is an important aspect of Nevada and western mining." (Finding 117; Tr., pp. 2266-69)

Similar statements came from the outstanding public service bodies of the mining industry: the American Mining Congress and the American Institute of Mining, Metallurgical and Petroleum Engineers, Inc. (Finding 118; Tr., pp. 2268-2274).

C. The Commission's Order Is Based Upon False Premises Not Supported by the Record.

1. The Commission Did Not Charge or Prove That Any Member of the Public Suffered Monetary Loss.

The Commission, in its "Findings and Opinion of the Commission", disposed of the uncontradicted and unchallenged evidence by the responsible public officials and public bodies with a single paragraph (at p. 11):

> "We have given consideration to the views expressed by several public officials and civic and business associations that the present Exchange has served a useful purpose and that it or one like it should be allowed to exist. We recognize that an area exchange, whether or not it is limited to trading in securities of mining concerns, may serve a valuable function, but we think we would not fulfill our duty to act for the protection of investors if we did not withdraw the registration of this Exchange, which as the hearing examiner found, has a history of 'pervasive and abysmal abdication of responsibility' and which because of its 'aura of legitimacy' as a quasi-public institution has been used as 'an unsuspected tool for manipulative practices perpetrated by its members and principal officers for their own personal and unconscionable gain.' The withdrawal of its registration is, if anything, long overdue."

It will be seen at once that the Commission's conclusion is based upon the premise that the Mining Exchange "has been used as 'an unsuspected tool for manipulative practices perpetrated by its members and principal officers for their own personal and unconscionable gain.'"

The fact is that the prosecuting Division did not charge or prove that any member of the public suffered mone-

tary loss by reason of any of the alleged violations. This was conceded by the Hearing Examiner, who specifically found that:

> "* * * It must be acknowledged that no evidence was introduced in this proceeding of specific losses sustained by the public." (at p. 106 of the "Recommended Decision")

This failure of the Division to charge or prove that any member of the public suffered monetary loss must be regarded as significant in a proceeding in which a review of the charges discloses that subordinates on the legal staff dredged up every single instance of the most technical and insignificant type of violation dating back as far as 1939, more than twenty-three years stale. It is certain that, had there been any instances of members of the public suffering monetary loss, they would have been charged.

A strong factor in favor of the conclusion of the Hearing Examiner as opposed to that of the Commission is the fact that, in all of its history of operation for more than one hundred years the San Francisco Mining Exchange had never previously been charged or cited by any enforcement or regulatory agency of any kind, Federal, state, or local. This fact was testified to without challenge by both the president of the Mining Exchange, George J. Flach (Tr., p. 2100) and its longtime secretary, Frank J. Carter (Tr., pp. 2200-01).

2. **The Commission Charged the Mining Exchange for Its Failure to Retain Legal Counsel—But It Closed Its Mind Against Him When He Sought to Confer About Rehabilitation.**

Another point that the Commission relied upon as a basis of its conclusion was the contention that:

> "The Exchange has been given an overabundance of opportunities to organize itself and operate in a manner consistent with its responsibilities under the law." (p. 9 of Findings and Opinion of the Commission)

One compelling answer to that argument is that, as the Commission itself charged and found:

> "Apart from the retention of counsel in anticipation of and in connection with these proceedings, the Exchange had never regularly retained or sought the advice of counsel." ("Findings and Opinion", p. 10)

The Commission thus exposes itself as criticizing the Mining Exchange for not retaining legal counsel and even cites that failure as a reason for terminating the registration of the Exchange. Yet, when the Mining Exchange first retained counsel, and he requested a conference to discuss a plan of rehabilitation, he was rebuffed crisply by the Associate Director of the Division of Trading and Exchanges, who wired:

"REHABILITATION IMPOSSIBLE."

D. The Mining Exchange Has Survived a Period of Four Years of the Most Severe Probation Without New Charges Being Filed.

At this date, almost four years later, it is a demonstrable fact that, since legal counsel was engaged by the Mining Exchange, it has not been charged or cited for any alleged violations of either statute or rule.

The Mining Exchange has survived a four year period of probation of the most severe type, and under the closest and most critical of scrutiny.

The record of the past four years of operation of the Mining Exchange supports the conclusion of the Hearing Examiner that a further opportunity for reorganization and rehabilitation, under the guidance of legal counsel, is in the public interest and warranted by the record.

Both the record of proceedings and the record of performance support the conclusion and the remedy of the Hearing Examiner and contradict those of the Commission.

The "Order Withdrawing Registration of National Securities Exchange" as entered on April 22, 1966 should be set aside. It should be modified by the entry of an order and judgment providing for a reorganization of the Mining Exchange in accord with the recommendations of the Hearing Examiner.

Such a reorganization should be under Court direction, not under the supervision of a strongly biased and prejudiced Commission.

VI. SUBSTANTIAL ISSUES OF LAW HAVE BEEN PRESENTED—THE STAY OF THE COMMISSION'S ORDER SHOULD BE EXTENDED UNTIL FINAL DETERMINATION.

Petitioner submits that in this, its "Petition to Review, Modify and Set Aside, and to Stay, an Order of the Securities and Exchange Commission", it has stated substantial issues of law requiring the consideration of this Honorable Court. It submits that, pending the final

determination of those issues, the stay heretofore granted by this Court by written order on May 3, 1966 should be continued in force and effect until such final determination, in order that the Commission's order terminating the registration of petitioner may be held in suspense pending that final determination.

Dated, San Francisco, California,
June 20, 1966.

Respectfully submitted,

GARDINER JOHNSON,
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JOHN M. ANDERSON,
Attorneys for Petitioner.

JOHNSON & STANTON,
Of Counsel.

CERTIFICATE OF COUNSEL

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

GARDINER JOHNSON,
Attorney for Petitioner.

(Appendix Follows)

Appendix.

SECURITIES AND EXCHANGE COMMISSION
Washington, D. C.
April 22, 1966

In the Matter of	
AN FRANCISCO MINING EXCHANGE	FINDINGS AND OPINION OF THE COMMISSION
File No. 10-38	
curities Exchange Act of 1934 - Section 19(a)(1)	

REGISTRATION OF NATIONAL SECURITIES EXCHANGE

Grounds for Withdrawal of Registration

Failure to Enforce Compliance with Exchange Act and Rules Thereunder

Public Interest

Where registered national securities exchange over period of years repeatedly failed and neglected to enforce compliance with Securities Exchange Act of 1934 and rules thereunder by members and by issuers of securities listed thereon, and lent its facilities to unlawful securities distributions; where its officials themselves engaged in repeated violations of that Act and Securities Act of 1933; and where Exchange does not perform any significant function as a trading market, held, necessary and appropriate for protection of investors to withdraw registration of Exchange.

Opportunity for Rehabilitation

Withholding order of withdrawal pending attempt at rehabilitation by Exchange found to have pervasive and serious deficiencies is not warranted where Exchange has failed to avail itself of prior opportunities to take corrective measures and where, if effective rehabilitation is to be achieved, complete reorganization and change of personnel constituting in effect organization of entirely new exchange would be necessary.

ARANCES:

Frank E. Kennamer, Jr., Edward B. Wagner and William P. Sullivan, the Division of Trading and Markets of the Commission.

Gardiner Johnson, of Johnson & Stanton, for the San Francisco g Exchange.

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Under Section 19(a)(1) of the Securities Exchange Act of 1934 hange Act"), this Commission is authorized, if in our opinion such

action is necessary or appropriate for the protection of investors, to withdraw the registration of a national securities exchange if we find that such exchange has violated any provision of the Exchange Act or of the rules thereunder or has failed to enforce, so far as is within its power, compliance therewith by a member of the exchange or by an issuer of a security registered thereon. These proceedings were instituted to determine whether or not withdrawal of registration should be ordered against the San Francisco Mining Exchange ("Exchange").

After appropriate notice, hearings were held before a hearing examiner at which the Exchange stipulated to and admitted many of the factual matters alleged in the order for proceedings and additional evidence was received with respect to certain of those matters. Thereafter proposed findings and conclusions and briefs were filed by our Division of Trading and Markets ("Division") and by the Exchange, and the hearing examiner issued his recommended decision.

The hearing examiner found among other things that there had been numerous and repeated violations involving issuers, members and officials of the Exchange; that the Exchange had not made any effort to enforce pliance by issuers or members with the Exchange Act or to enforce its rules adopted pursuant to the Act; that the Exchange had been a vehicle for evading and circumventing provisions of the securities acts designed for the protection of investors and in the public interest; and that remedial action must be taken in the public interest. The examiner, however, upon consideration of statements received from various public officials and others, and considering the Exchange as an institution distinguishable from its management, recommended that the Exchange be given a further opportunity to effect a complete reorganization and that if failed to do so within 90 days the registration of the Exchange be withdrawn forthwith.

The Division filed exceptions and a brief urging that the registration of the Exchange be withdrawn. The Exchange excepted to a limited number of the hearing examiner's findings but only insofar as they might state or imply that the Exchange was not interested or willing to consider and effect an appropriate reorganization, and the Exchange supported the hearing examiner's recommendation that it be given a further opportunity to reorganize.

After hearing oral argument and on the basis of an independent review of the record we make the following findings.

The Exchange, an unincorporated business association, has been registered pursuant to Section 6 of the Exchange Act since June 1, 1936. 1/ George J. Flach has been president of the Exchange since 193 and Frank J. Carter was secretary from 1936 and chairman of the Stock List Committee from 1950 until his death in 1965. Raymond A. Br has been treasurer since 1933, a member of the Governing Committee sin 1936, and a member of the Stock List Committee since 1950. Archie H. Chevrier was a member of the Governing Committee and the Stock List Committee from 1957 until 1962, and he was vice president of the Exchange and Chairman of the Governing Committee for a short period of time unt he resigned these positions in March 1962. His offices were taken ove first by Walter D. Forsyth, who had been a member of the Governing Committee since 1944, and subsequently in April 1962 by Paul W. Schwarz w

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1/ The Exchange was first organized in 1862 under the name of the San Francisco Stock and Exchange Board. It took its present name in 19

rior occasions going back to 1951 had served as vice president of the hange and chairman of the Governing Committee.

As of December 1962 the Exchange had 13 regular members, of whom six were actively engaged in the securities business, and those six d as representatives of three registered broker-dealer firms. Flach, an Hudson and Samuel Apple represented R. L. Colburn Co. ("Colburn"), rporation with offices in Los Angeles and San Francisco; 2/ Broy and or J. Herrman represented the Broy Company, a sole proprietorship; Forsyth traded as a sole proprietor until his death in 1963. In nt years almost all of the active trading on the floor of the Exchange conducted by Flach, Broy, Herrman and Chevrier. Aside from Carter, Exchange had only one salaried employee, the brother of Flach, whose tions were to work the blackboard during trading sessions, deliver k and prepare daily quotation sheets and monthly summaries. During an average of 42 stocks, having an average price per share of 14¢, listed for trading on the Exchange. Of these 42 listed companies, least 15 had no revenue, and 8 others had revenue of less than $1,000. four listed companies had net earnings, and three of these had ing markets through listings on other exchanges. Of the 42 companies, id not have a book value of more than 1¢ per share, and nine of these no book value at all. Of the remaining 26 companies, 24 had a book e of 20¢ or less per share. As of December 1962, 25 of the 42 com- es were not actively engaged in operations.

Most of the facts found by the hearing examiner with respect to operations of the Exchange and the violations are not disputed. We t his findings of fact and repeat and summarize them here to the ex- necessary to give a full understanding of the issues presented to us.

ure to Take Action With Respect to Violations by ssuers and Exchange Members

Various issuers of securities registered on the Exchange failed gether to file or filed late the annual and interim current reports ired by the Exchange Act and the rules thereunder. 3/ In some nces the violations by a particular issuer occurred repeatedly over years. The Exchange took no steps to enforce compliance with the rting requirements, despite the fact that repeated violations were ous on the face of reports filed late and any failure to file an al report was evident from the Exchange's own records, and despite rous warning letters by our staff to Carter as secretary of the nge calling attention to the violations.

Thus, the annual reports of Operator Consolidated Mines Company erator") for 1942, 1943, 1944, 1945, 1946 and 1950 were filed late eriods ranging from two months to seven months. Operator also failed ile any current reports in 1956 with respect to an assessment levied nst its outstanding shares, the sale of certain shares for which the ssment was not paid, and a charter amendment increasing its autho- d shares from 3,000,000 to 10,000,000. Flach was Operator's presi- and a major stockholder and Carter was a holder of Operator stock these reporting violations occurred.

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olburn's main office is in Los Angeles; Flach has been employed as anager of its San Francisco branch office.

ection 13(a) of the Exchange Act and Rules 17 CFR 240.13a-1 and 3a-11 thereunder require every issuer of a security registered on a ational securities exchange to file, with this Commission and with he exchange, an annual report within 120 days after the close of

(Continued)

Reorganized Carrie Silver-Lead Mines Corp. was late in filing annual reports for 1939, 1940, 1942, 1944, 1945 and 1946 by periods o two months to 11 months. Consolidated Virginia Mining Co. ("Consolidated") was late in filing its annual reports for 1953, 1955 1957 and 1958, the delinquencies ranging from one month to seven mont Consolidated also failed to file a current report in 1956 with respec to its issuance of over 12,000,000 shares of its stock in exchange fo the stock of Hampton Mining Co. Eureka Company failed to file an ann report for 1955. On the basis of some of these delinquencies as well other violations of the Exchange Act, this Commission itself ultimate withdrew the securities of these four issuers from registration on th Exchange. 4/

Ambrosia Minerals, Inc. ("Ambrosia") filed an application with Exchange for registration in May 1956 which contained financial state ments certified by an accountant who was secretary-treasurer of the c pany and accordingly was not independent as required. Flach and Cart were both acquainted with officials of the company, and after the app cation for listing had been filed and before it was approved Flach re ceived an option to purchase 6,000 shares of Ambrosia stock, but they did not note or take corrective action with respect to the deficient financial statements. Subsequently we withdrew the registration on t Exchange of the Ambrosia stock because of Ambrosia's failure to compl with registration and reporting provisions of the Exchange Act. 5/

As we noted in two of the proceedings in which we found it nec sary to initiate action to delist securities registered on the Exchan delays and failures to comply with reporting requirements can not onl frustrate the statutory objective of keeping existing and potential investors informed of material corporate activities and events, but a can serve to help conceal public distributions of unregistered securi ties in violation of the Securities Act of 1933 ("Securities Act"). 6 The record in the instant proceedings shows how in other instances th Exchange's failure to require compliance with the Exchange Act by its members or issuers also led to or facilitated violations of the Securities Act.

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3 contd./

each fiscal year, and a current report within 10 days after the cl of each month during which there occurs any of a number of specifi events which are considered material information for investors.

4/ Operator Consolidated Mines Company, 39 S.E.C. 580 (1959); Reorgan Carrie Silver-Lead Mines Corporation, 29 S.E.C. 49 (1949); Consoli dated Virginia Mining Company, 39 S.E.C. 705 (1960); Eureka Compan 38 S.E.C. 475 (1958). The Exchange suspended trading in the Opera and Eureka stocks, but only after the institution of our proceeding against those companies.

5/ 39 S.E.C. 734 (1960).

6/ Eureka Company, 38 S.E.C. 475, 483-484 (1958); Consolidated Virgin Mining Company, 39 S.E.C. 705, 709 (1960).

In 1954 Chevrier acquired control of Comstock, Ltd. ("Comstock"), an inactive corporation with virtually no assets, and he became ident and Carter vice president. With the assistance of Carter, rier caused the Comstock stock to become registered and listed on Exchange in 1955. In 1956 Chevrier entered into an agreement for nerger of Comstock with a company in the charcoal business. In ection with such agreement Chevrier purported to sell a controlling k of 500,000 shares of Comstock stock to six persons but under cir- tances whereby the alleged purchasers merely received an option to hase the shares and Chevrier still remained the beneficial owner eof. Nevertheless Comstock filed with us and the Exchange a current rt in February 1957 falsely reporting the transactions as a sale, the obvious purpose, as the hearing examiner found, of having it ar that neither Chevrier nor any of the six purported purchasers was beneficial owner of 10% or more of the outstanding stock. Carter, received the report as an officer of the Exchange, knew or should known of the false or misleading nature of the report in view of connections with the issuer. Thereafter during 1957 H. Carroll & ("Carroll"), a registered broker-dealer, made a public distribution mstock shares, obtaining the shares it sold to the public from the olling block of 500,000 shares optioned by Chevrier and also from s purchased on the Exchange by Chevrier. Chevrier purchased over 00 shares on the Exchange for Carroll's account in a two month d during which the stock's price increased by more than 40%, there- anipulating the price in such a manner as to facilitate the over-the- ter distribution being conducted by Carroll.

In the distribution of the Comstock shares false and misleading sentations were made in violation of the anti-fraud provisions of Securities Act and of the Exchange Act. Carter as secretary of the nge received a letter sent by Comstock to its stockholders and a ure used by Carroll, both of which contained misrepresentations as mstock's assets and prospects, but he did nothing. Only after ning that the matter was under investigation by our staff did the nge suspend trading in Comstock shares. 7/

Finally we note that Comstock's annual reports for 1955 and 1956 not contain the required financial statements due to the fact that, result of dissension that had arisen between Chevrier and the group cted with the charcoal company, Chevrier had retained and refused turn certain corporate records. Although Carter received a copy of ter from Comstock to Chevrier demanding the return of corporate ds and an application to the Exchange by Comstock for delisting of tock stated that the wrongful withholding of records by Chevrier principal reason for Comstock's inability to comply with the report- requirements, neither Carter nor the Exchange made any inquiry or tigation of the charges against Chevrier and took no action in re- thereof.

In 1960 Chevrier was president, director and a principal stock- r of Best & Belcher Gold and Silver Mining Corporation ("Best and ner"), a company whose stock was registered on the Exchange but which been dormant for about 20 years and which had net assets of $2,943,

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subsequently revoked Carroll's registration as a broker-dealer sed on findings, among other things, of violations of the regis- ation and anti-fraud provisions of the Securities Act and the change Act in the offer and sale of Comstock shares. H. Carroll Co., 39 S.E.C. 780 (1960).

current assets of $609, and current liabilities of $6,901. As part o plans to merge certain other companies with a company whose stock was registered on the Exchange, and in order to avoid certain restriction arising from the fact that Best & Belcher was incorporated in Califor Chevrier in October 1961 caused Industrial Enterprises, Inc. ("Industrial") to be incorporated in Nevada, and thereafter caused Be & Belcher to become merged into Industrial. Chevrier and Arnold Toew another member of the Exchange, became directors of Industrial, and t Industrial stock was listed on the Exchange in place of the Best & Belcher stock. Chevrier, for his own and family accounts and as agen for certain non-member brokers, engaged in heavy trading in Best & Belcher stock on the Exchange prior to the merger, and the price of t stock went from 17¢ in September 1961 to $1.75 per share in December.

In December 1961 Industrial acquired a controlling interest in Caloric Foods, Inc. ("Caloric"), a promotional company which allegedl owned certain formulas for the production of low calorie diets. In c nection with such acquisition Industrial issued 750,000 shares of its stock. In January 1962 the Exchange approved the registration and li ing of the additional 750,000 shares, despite the absence of certifie financial statements of Caloric in the listing application. Thereaft trading in the Industrial stock took place at prices increasing from about $1.75 to $2.25 per share, and it led Schwarz to advise our regi staff of what he considered the unusual activity and market behavior the Industrial stock and of the fact that Chevrier was touting that s After our staff began an investigation, the Exchange rescinded its ap proval of the supplemental listing of the 750,000 shares, and we sus- pended trading in the Industrial stock on the Exchange. 9/

The Best & Belcher-Industrial situation presents an example, a the hearing examiner found, of the use of a "corporate-shell game," b an official of the Exchange, who engaged in a scheme whereby, through merger and manipulative trading on the Exchange, the stock of a long dormant company was raised from about 17¢ per share to $2.25 per shar in about five months, to the substantial profit of the Exchange offic and others, and in violation of the registration, anti-fraud and othe provisions of the Securities Act and of the Exchange Act. 10/

8/ A total of only 5,000 shares of Best & Belcher shares was traded the Exchange in the nine months January - September 1961, of whic 3,000 had been purchased in September by Chevrier. Trading in November reached a total of 68,940 shares, with Chevrier purchasi 47,100 shares and selling 54,140 for his various accounts.

9/ After successive orders by us pursuant to Section 19(a)(4) of the Exchange Act suspended trading on the Exchange from March to Octo 1962, the Exchange made an application, which we granted, to stri the Industrial stock from listing and registration on the Exchang

10/ In June 1962 the Exchange suspended Chevrier pending the outcome administrative proceedings instituted against him under the Excha Act. Subsequently, we revoked Chevrier's registration as a broke dealer and expelled him from the Exchange on the basis of findin that he had engaged in a manipulative scheme with respect to the Best & Belcher-Industrial stock, filed false reports and failed t file required reports under Section 16 of the Exchange Act, con- firmed transactions as agent and charged commissions when acting as principal, and falsified his records. Securities Exchange Ac Release No. 7579 (April 22, 1965).

In May 1961 the Exchange approved a supplemental listing of 00 shares of stock of Apex Minerals Corporation which had been d to a promoter of the company who also became its president, and in associates. The listing application claimed that these shares exempt from registration under the Securities Act on the ground they had been "acquired for investment only and not for resale or ibution." Nevertheless, both before and after the supplemental ng Broy, who was then a member of the Exchange's Stock List and ning Committees, sold a substantial number of these shares on the nge for the account of Apex's promoter-president, under circum- es which, as the hearing examiner found, constituted an illegal distribution of unregistered stock in violation of Section 5 of ecurities Act.

In 1957 the Exchange received an application for the listing and tration of stock of Wilson Oil and Gas Company ("Wilson"). The cation stated that the company had been incorporated in 1956, and in that year 7,500,000 shares had been sold through H. Carroll & Co. sidents of Colorado, and that such sale constituted an intrastate ibution exempt from registration under the Securities Act. Although xchange received information that a number of stockholders had sses in states outside of Colorado, the Exchange approved the listing ut making any inquiry or investigation as to compliance with the ities Act. 11/

The Exchange maintained no procedures for discovery and prevention olation of Regulation T issued by the Board of Governors of the al Reserve System under Section 7 of the Exchange Act. In over 25 of the Exchange's existence only about 100 requests for extensions ne for receipt of payment were made to it by its members. In the ancisco office of R. L. Colburn Company managed by Flach an inspec- n 1962 disclosed 55 instances in which credit had been illegally ed by Flach, with the periods of delinquency in which no action was to cancel or liquidate transactions in which payments were not re- d within the prescribed time ranging up to 12 years. 12/

In addition, in numerous instances Flach and other members and als of the Exchange failed to comply with the reporting requirements tion 16(a) of the Exchange Act and Rule 17 CFR 240.16a-1. 13/ For

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hen the above facts became known to our staff, it requested and se- ured withdrawal of the Exchange's certification of listing of the lson stock.

bsequently in administrative proceedings before us we found that lburn, aided and abetted by Flach, extended credit in willful vio- tion of Section 7(c) of the Exchange Act and Regulation T as well failed to notify customers that it was acting as broker for both yer and seller, and in addition to suspensions against the firm, found Flach to be a cause of the firm's suspensions and suspended m from the Exchange for 90 days, R. L. Colburn Company, Securities change Act Release No. 7547 (March 9, 1965).

applicable here, these provisions require owners of more than 10% a class of equity securities registered on a national securities xchange and officers and directors of the issuer of such security, file with this Commission and the appropriate exchange, reports their beneficial ownership of equity securities of such issuers d of any changes in such ownership.

example, in the period 1941 to 1959 Flach in 16 instances failed to fi on time required reports of his holdings of and transactions in stock Manhattan Gold Mines Co. ("Manhattan") and Operator during times when was president and a director, respectively, of those companies. The d lays in filing such reports ranged up to 34 months. In the period 194 to 1960, Schwarz, while an officer and a director of Manhattan, Pony Meadows Mining Co. ("Pony"), Silver Divide Mines Co., Smuggler Mining Co., Ltd., and Comstock-Keystone Mining Co., failed to file required reports in five instances and in five other instances filed reports which were late by periods ranging up to 31 months.

From 1958 to 1962 Chevrier as president and director of Industrial and a principal stockholder of Pony, failed in four instanc to file reports and in eight other instances filed reports which were late by periods ranging up to three months. In five instances reports which were filed were false or incomplete in that they did not disclos the full extent of his holdings and transactions. From 1955 to 1959 Toews, as an officer and director of Comstock, Industrial and Sunburst Petroleum Corp., failed to file two reports and filed four reports whi were late by periods up to seven months.

Again, although these officials and members of the Exchange wer repeatedly in violation of the reporting requirements of Section 16(a) of the Exchange Act, and the reports filed late with the Exchange disclosed on their face the delinquencies involved, the Exchange took no disciplinary action nor made any efforts to enforce compliance.

As the foregoing shows and the hearing examiner found, the Exch over a long period of time failed to enforce compliance with the Excha Act and the rules thereunder by its members and by issuers of securiti registered thereon. The violations were numerous and repeated, and we not only known to the Exchange and its officials, but various official of the Exchange were themselves involved in violations.

The Exchange has an essential obligation to make sure that its members observe the standards of conduct required by the Exchange Act. The self-policing function of a registered national securities exchang is of the utmost importance in fulfilling the statutory scheme of cooperative regulation of the securities markets in the interest of pr tecting the public. Section 6(a) requires as a condition of registration as a national securities exchange an agreement, which the Exchange here supplied, to comply and to enforce, so far as within its powers, compliance by its members with the provisions of the Exchange Act and rules thereunder. Further, Section 6(b) requires, and the Exchange's constitution includes, provisions for the expulsion, suspension or disciplining of a member for conduct inconsistent with just and equitable principles of trade and for the willful violation of any provision of the Exchange Act or any rule thereunder.

The self-regulatory responsibilities imposed on a securities exchange cannot be fulfilled merely by adopting regulations for disciplining its members; Section 6(b) imposes the further duty upon the Exchange of enforcing its own disciplinary provisions. 14/ Notwithstanding the numerous violations of the Exchange Act by members of the Exchange, some of which have been detailed here, in more than ten year the only disciplinary actions taken by the Exchange were to fine

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14/ See Baird v. Franklin, 141 F.2d 238 (C.A. 2, 1944), cert. denied 323 U.S. 737 (1944); Avery v. Moffett, 55 N.Y.S. 2d 215 (1945); cf. Pettit v. American Stock Exchange, 217 F. Supp. 21 (S.D.N.Y., 1963).

evrier for the use of intemperate language, and to suspend Chevrier in 62 following the institution by us of disciplinary proceedings against m. The Exchange, itself, thus totally abdicated its vital self-gulatory function required by Section 6(b) of the Exchange Act.

Public Interest

We have found that the Exchange has violated the Exchange Act and s failed to enforce compliance therewith by its members and by issuers securities registered thereon. In the light of all the surrounding rcumstances there is ample basis for concluding, as the hearing aminer did, that remedial action is required. Indeed, the Exchange es not except to this conclusion. Rather, it recommends that the Ex-ange be given another chance to set its house in order. We cannot ree, and in our opinion it is necessary and appropriate for the pro-ction of investors to withdraw its registration.

The Exchange has been given an over-abundance of opportunities to ganize itself and operate in a manner consistent with its responsibili-es under the law. 15/ Over the years, in addition to the numerous tters from our staff with respect to reporting violations, it has been cessary for us to withdraw the registrations on the Exchange of the curities of 28 issuers on the basis of findings of violations of various ovisions of the securities acts which made such delistings necessary and propriate for the protection of investors. In 1957, after the institu-on during that year of four proceedings which subsequently resulted in listing orders on the basis of findings of violations of the reporting d proxy soliciting requirements, 16/ our staff made specific written

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/ In fact, in 1935 in connection with proceedings relating to the Exchange's registration as a national securities exchange under the Exchange Act, a hearing examiner in his recommended decision stated:

> "It is the conclusion of the Trial Examiner that the San Francisco Mining Exchange had been negligent, to the time of the hearing above referred to, in adopting and enforcing rules looking toward fair trading in securities listed upon the Exchange. It seems probable that registration of the Exchange as a national securities exchange will give an opportunity for a thorough-going revision, by the Exchange, of its rules, and in the opinion of the Trial Examiner registration of the San Francisco Mining Exchange as a national securities exchange would at least afford the opportunity for a rehabilitation of said Exchange."

The record in the instant proceedings is a sad commentary on the willingness and ability of the Exchange in the intervening years to rehabilitate itself.

/ Verdi Development Company, 38 S.E.C. 553 (1958); Eureka Company, 38 S.E.C. 475 (1958); Operator Consolidated Mines Company, 39 S.E.C. 580 (1959); Consolidated Virginia Mining Company, 39 S.E.C. 705 (1960). In March 1957 the promoters of Operator were also enjoined from selling unregistered securities in violation of Section 5 of the Securities Act.

recommendations to the Exchange as to changes in rules and procedures sidered necessary to enable the Exchange to meet the standards applica to a registered national securities exchange. The Exchange up to 1962 adopted only some of these recommendations and partially carried out others. It took no action with respect to some recommendations, inclu ing those for the supervision of members' personal trading, the delist of the securities of dormant and inactive issuers, and the improvement listing standards.

Apart from the retention of counsel in anticipation of and in c nection with these proceedings, the Exchange had never regularly retai or sought the advice of counsel. Not until 1962, when these proceedin were imminent, did the Exchange's Governing Committee hold a formal me ing to consider implementation of the written recommendations submitte by our staff in 1957. The Exchange has never made an independent inve gation of the financial condition of applicants for listing or employe a certified public accountant to examine or advise with respect to fi- nancial statements in listing applications or reports.

The Exchange's listing standards are minimal to the extreme, 17/ and even so they have not been uniformly observed. It has no organiza tion worthy of the name; we have already noted that over the years it had only two salaried employees, Carter and one other employee, and on the Governing and Stock List committees ever actually met, with the latter committee rarely if ever holding a separate meeting. Furthermo the Exchange does not perform any substantial or significant function a trading market. As has been stated, as of December 1962 there were only 13 members, of whom only six were active in the securities busine the stocks listed on the Exchange had little or no underlying income o book value, and many of the issuers were dormant. Trading volume on t Exchange is small.

In view of this history of failure to prevent or punish violati inadequate and careless procedures, inadequate standards and organizat and dormant and marginal listed companies, it is evident that there is really nothing of substance to salvage of the present Exchange. It is also evident that the Exchange's principal contribution in recent year has been to provide an exchange registration and listing to some issue which had no other assets to speak of and thereby facilitate, thrbugh the Exchange mechanism, and in some instances with the knowledge or active participation of Exchange officials, illegal and fraudulent dis tributions of worthless or highly speculative securities to the public

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17/ Issuers were required to show only that 15% of their outstanding shares were publicly owned and that they had at least 100 public shareholders.

18/ In Operator Consolidated Mines Company, 39 S.E.C. 580, 594 (1959), we stated: "The situation here presented is one where a dormant insolvent corporation, whose chief value lay in the registration a listing of its stock on the Exchange, was reactivated by a group which accumulated various properties to be transferred to the regi trant in exchange for large blocks of its stock. Most of the prop erties were undeveloped or of a speculative nature and in large measure were subsequently abandoned. The large blocks of stock issued in exchange therefor were not registered under the Securiti Act and were issued without any restrictions or precautions to pre vent illegal public distribution of unregistered securities, and i fact some of those shares were involved in a public distribution without the disclosure and safeguards inherent in registration und the Securities Act."

Any "reorganization" of this mere facade of an exchange would of ssity involve the creation of ar entirely new structure, retaining ing of the old form except possibly its name. The hearing examiner elf stressed that any reorganization must include "all functional cts" and present "entirely new personnel in every department of gement without exception." Such a "reorganization" would in es- be the withdrawal of the registration of the present Exchange and registration of a completely new exchange. We recognize this lty by withdrawing the registration of this Exchange.

We have given consideration to the views expressed by several lc officials and civic and business associations that the present ange has served a useful purpose and that it or one like it should be ved to exist. We recognize that an area exchange, whether or not it imited to trading in securities of mining concerns, may serve a able function, but we think we would not fulfill our duty to act for protection of investors if we did not withdraw the registration of Exchange, which as the hearing examiner found, has a history of vasive and abysmal abdication of responsibility" and which because cs "aura of legitimacy" as a quasi-public institution has been used in unsuspected tool for manipulative practices perpetrated by its ers and principal officers for their own personal and unconscionable ." The withdrawal of its registration is, if anything, long over- 19/

An appropriate order will issue.

By the Commission (Chairman COHEN and Commissioners WOODSIDE, , BUDGE and WHEAT).

Orval L. DuBois
Secretary

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he Exchange in its brief in support of the hearing examiner's recom- ended decision states that if his recommendation is not approved by is, its position is that it has been denied a full and fair hearing ecause of our refusal to authorize the issuance of subpoenas directed to the members of this Commission and our Secretary and for the pro- uction of non-public Commission files, all allegedly for the purpose f inquiring into whether this Commission was biased or had prejudged he issues against the Exchange. We have already considered and re- ected these contentions of the Exchange on three prior occasions. ecurities Exchange Act Release No. 7106 (July 31, 1963); Securities xchange Act Release No. 7136 (September 9, 1963); Securities Ex- hange Act Release No. 7247 (February 26, 1964). We see no reason to hange our conclusions in this respect and for all the reasons stated n our prior rulings we affirm them. Nothing has been presented to ndicate that the Exchange has not had a fair hearing. In fact, as e previously noted (Securities Exchange Act Release No. 7106, p. 2) n view of the nature of these proceedings we authorized the Division o take the unusual step of furnishing the Exchange a copy of the ivision's investigation report prior to the institution of these roceedings. Our decision herein is based solely on the facts in his record, many of which have been admitted by the Exchange and ost of which are uncontroverted.

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION
April 22, 1966

In the Matter of SAN FRANCISCO MINING EXCHANGE File No. 10-38 Securities Exchange Act of 1934 - Section 19(a)(1)	ORDER WITHDRAWING REGISTRATION OF NATIONAL SECURITIES EXCHANGE

Proceedings were instituted pursuant to Section 19(a)(1) of t Securities Exchange Act of 1934 to determine whether to withdraw the registration as a national securities exchange of the San Francisco Mining Exchange.

Hearings were held after appropriate notice, the hearing exam submitted a recommended decision, exceptions thereto were filed by t San Francisco Mining Exchange and the Division of Trading and Market the Commission, and oral argument was presented to the Commission.

The Commission has this day issued its Findings and Opinion herein; on the basis of said Findings and Opinion

IT IS ORDERED, pursuant to Section 19(a)(1) of the Securities Exchange Act of 1934, that the registration as a national securities exchange of the San Francisco Mining Exchange be, and it hereby is, withdrawn, effective at the close of business April 29, 1966.

By the Commission.

Orval L. DuBois
Secretary